

WILL "MANAGED CAPITALISM" PULL US THROUGH?

Balance Sheet of Two Decades of Keynes

J. K. GALBRAITH

"TO UNDERSTAND my state of mind," Keynes wrote George Bernard Shaw in 1935, "... you have to know that I believe myself to be writing a book on economic theory which will largely revolutionise—not, I suppose, at once but in the course of the next ten years—the way the world thinks about economic problems." No man has ever written a book above the pretensions of a home repair manual who did not at some moment feel that he was on the edge of greatness, and few books would be finished without the support of this delusion. Keynes, however, spoke with foresight. His *General Theory of Employment, Interest and Money*, which appeared the following year, did change, far more than any other book of the first half of the century—and in the current of evolutionary as distinct from revolutionary economics, more than any book since Ricardo's *Principles of Political Economy*—the way men think about economics. His only substantial error was in his estimate of the time that would be needed for his ideas to take hold. There was resistance, but if bitter it was brief. Long before Keynes's death, almost exactly ten years after the publication of the *General Theory*, Anglo-American thinking on economics had been deeply

and permanently reshaped by his book. Implicitly and in large measure explicitly, his ideas were those by which the English-speaking countries sought to guide their economies. The name of Keynes and the notion of a liberal but *guided* capitalism had become largely synonymous.

In view of his influence, Keynes, though by no means an obscure, is still a relatively unknown figure. Everyone has some sort of working knowledge of the career of Marx; it is my impression that the devout still worry their way through his books, or at least the abridged versions, for reasons of duty if not of comprehension. There are hundreds of thousands of Keynesians who know Keynes only as a remarkably versatile Englishman, rather recently dead, who objected brilliantly to the reparations clauses of the Versailles Treaty and who established a reputation during and immediately after the Second World War as a negotiator with the United States. The *General Theory* has been read by only the merest handful of laymen. Indeed, among non-mathematical works on economics, it is for the lay reader almost uniquely incomprehensible. Hundreds have bought the book with a fine determination to get to the original sources of a doctrine they find themselves accepting or even espousing. After being warned on, say, page 25, that "the value of D at the point of the aggregate demand function, where it is intersected by the aggregate supply function, will be called *the effective demand*," they have postponed their education until a day of greater leisure, meaning forever. Even professional economists have found it more convenient to teach from one or another of Keynes's numerous interpreters than from the master. Partly for this reason, an inquiry among professing Keynesians as to his principal contribution to economics would bring forth a notable variety of an-

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FOR anyone who wants to know about Keynes, the scholar, public official, essayist, patron of the arts, journalist, speculator, and businessman—who wishes, in brief, to follow one of the most varied and interesting lives of modern times—a full-length biography is now available.* It is not in all respects a good one. The author, R. F. Harrod, would seem to have been the nearly ideal selection for what amounts to the authorized story of Keynes's life. (He had access to Keynes's papers and the generous assistance of Keynes's parents and friends.) Mr. Harrod is an economist, an early disciple of Keynes, and of course he knew Keynes well. However, it is the task of the biographer to deal with his subject and forget himself. Of such an exercise in self-effacement Mr. Harrod, unhappily, shows himself to be incapable. He yields to the temptation to walk through the pages side by side with Keynes and, all too frequently, to climb on the shoulders of his great friend to enjoy a little of the limelight himself. When Keynes recedes and Harrod appears, the reader will almost certainly feel disappointed. For while Keynes was a citizen of the world, although no less an Englishman for the fact, Mr. Harrod's universe is a quadrilateral, the corners of which are Cambridge, London, Eton, and Oxford. His view of the intellectual life of the two old universities has something of the quality and all of the exclusiveness of an Ohio State alumnus contemplating the next football game with Michigan.

Nonetheless Mr. Harrod's portrait of Keynes is a striking one. The reader has a full view of the vitality, even majesty, of a man who crowded several lives into one. These were lives, incidentally, which were lived simultaneously. We are all acquainted with men who have run through several successful careers set end to end. But at any given time, Keynes was teaching, writing, making

money for himself, an insurance company, and King's College, Cambridge (of which he was long the bursar), directing a theater, running a farm, and counseling the British Treasury. He did nothing badly and only the last seems ever to have made anything like a preclusive claim on his energies.

Yet one does not sense that all this was wholly an accident of great ability, diligence, and personality. These Keynes possessed, but equally he was the product of an environment and an education which made the full development of his talents probable if not inevitable. He was, like John Stuart Mill, the son of highly educated parents. His father, John Neville Keynes, who survived him, was an eminent logician and a pioneer student of the formal methodology of economics. His mother, an equally remarkable person, was a warm and effective humanitarian. From this home and its rich and disciplined intellectual life Keynes went on to Eton and to King's College. No one ever had a better education by English standards or was better situated to profit from it. It may be there was never a much better education for those fortunate enough to have it. The British have never, as have we, sacrificed substance for seeming relevance and depth for superficial breadth. The successful product of this education knows the classics, not about them, the literature and history of his land, arithmetic, algebra, and geometry and, before all, English grammar. If a man has capacity for something more he has everything on which to build.

He has also, it would appear, a certain inner discipline which enables him, among other things, to stand success. Keynes is an admirable case in point. In the First World War, while still in his early thirties, he managed Britain's external finances for the Treasury and made a brilliant reputation in doing so. Then he went on to Paris with Lloyd George whence he returned to publish his great polemic against the Versailles Treaty, *The Economic Consequences of the Peace*. Immediately he was a world figure.

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ican. If a public servant or publicist he would probably have turned to active politics. After his reputation for global wisdom had dimmed he would turn up in Washington as a consultant. Or he might spend the rest of his life as a columnist, an *ad hoc* commentator or some other kind of road-company oracle, in any case sternly avoiding any further serious work. It is plain that the generality of our novelists, when endowed with the pecuniary rewards of great success, invest them in alcohol. For two decades Keynes was as firmly excluded from government service as an equally controversial man would be excluded from Washington. But he went on to conquer new worlds. The achievement with which he will be permanently identified, the *General Theory*, did not appear until he was fifty-three.

I HAVE said that a distinctive feature of Keynes's economics is its tendency to be—though not all things to all men—different things to many different men. The reason is simple. Keynes's impact on the world was on three different levels. There was first his technical analysis—his system of economic theory. Second there were the conclusions concerning the economy which derived from this analysis. These concerned, in particular, the behavior that might be expected of a liberal capitalist economy if left to itself. Third and finally there were the remedies for the defects of capitalism, most of them in the sphere of government policy, which were suggested by the analysis and conclusions. Depending on their interests and temperaments, Keynes's interpreters have concerned themselves with his analysis, his conclusions, or his remedies. Sometimes they have jumbled all three. The first step toward an appreciation of Keynes's economics consists simply in knowing about which of the foregoing one is talking.

The overwhelmingly important—and only superficially pessimistic—conclusion from Keynes's economics is that unemployment (and, by some extension of the analysis, also bouts of inflation) are as normal in a modern capitalist economy as stable full employment.

Keynes's analysis concerns itself with the way capitalism maintains its adjustment between its internal income-flows. Such adjustments are as inevitable as the fact that when one man spends money he affects the income of another. Keynes's major contribution here was in showing the importance of changes in the *total* output of the economy as a factor in making such adjustments. Thus it had once been supposed that, when people sought to save more than others sought to invest, a fall in the rate of interest would discourage intending savers and encourage intending investors and thus maintain the balance between savings and investment. Keynes contended that a fall in total production, by diminishing or frustrating intentions to save and producing involuntary investment, especially in inventories, was what maintained the balance. He similarly attacked, although somewhat more equivocally, the notion that a fall in wages would expand employment. It follows that if changes in total output (and therewith in employment) are one of the ways by which the economy keeps itself in adjustment during change, one can no longer suppose that this economy will have stable full employment as its norm.

At first glance this seems like wretched news. Also it was presented to the world in 1936 in the sixth year of a severe and exceedingly pertinacious depression. Keynes's conclusion thus seemed to confirm what most people had come to suspect, namely that the depression could be permanent. Conservatives, who had taken shelter behind the self-liquidating contention that all depressions were temporary and that the appropriate remedies were patience and resignation, thus had good reasons to dislike Keynes. Economic theory as well as the clock and calendar now became their enemy. Their suspicion that Keynes was somehow a radical and even sinister figure undoubtedly traces in part to this attack in their hour of despair. However, for a vastly greater number in the English-speaking countries he promptly emerged as a figure of hope. The reason lay not with either the theory or its practical conclusions but with the remedy that Keynes proposed.

IF depression comes as the result of total production being reduced to keep savings in line with a diminished volume of investment, then it follows that anything that increases investment, and hence production, will check and even reverse the decline. In principle, government borrowing and spending will be just as effective as private borrowing and spending. Should there be too strong a tendency in the opposite direction—should investment exceed current savings when the economy is working at capacity with a consequent tendency for prices to rise—higher taxes and a government surplus would check such inflation. None of this involved any detailed interference with private business or consumer decision. The only new function of the state was, by expanding demand, to provide such a setting for private decision that the latter, though quite uninhibited, would contribute to keeping the economy stable at or near full production levels.

None of this is so easy in fact as it has here been made to sound, nor nearly so easy as many of Keynes's disciples were at first inclined to think. Moreover in both Keynes's mind and theirs, the clear and present danger to capitalism was depression; it was in terms of depression that the Keynesian remedies were thought through. As I shall suggest in a moment, inflation, once dismissed as a rather academic threat, poses some uniquely stubborn issues of its own. The consequence of the *General Theory*, nonetheless, was an all-embracing change in attitudes toward capitalism.

There can be little doubt that prior to 1936 the common denominator of capitalist criticism was the view—more often perhaps implicit than explicit—that capitalism itself was temporary. Not unnaturally this view had come later to America than to Europe—greater youth and less faith in Marxian prophecy were both factors—but it came with a rush in the 30's. The depression bore a marked resemblance to the capitalist crisis. Germany, Italy, and Japan were all too obviously transmuting economic weakness into virulent nationalism. England, the United States, and the British commonwealths, with

their greater political capacity, were merely showing their greater ability to endure. It seemed uncomfortably probable that they too would one day face what the John Strachey of the day pictured as *The Coming Struggle for Power*. Whatever form this eventual transfiguration of capitalism might take, it did not seem possible that it could be accomplished by peaceful and orderly process.

KEYNES's achievement amounted to nothing less than a complete defeat of this fatalism. The action he proposed was well within the scope of democratic arbitrament. Indeed, if anything it looked too simple; those who had long since resigned themselves to the notion that capitalism was heading for some ill-defined but truly dramatic denouement could wonder if they weren't being suckers for a soft solution. The fact remained that within a decade the only people who still believed in the inevitability of a harsh solution for the instability of capitalism were those who preferred such a solution. In the West grounds for a faith in political gradualism had been once more established.

All of this explains Keynes's error in estimating the resistance to his ideas. All of his life, as Mr. Harrod makes clear, Keynes was profoundly persuaded of the inability of most men to change their minds. He had no trouble changing his own. The *General Theory* sharply reverses direction on his *Treatise on Money*, a great two-volume work published only a few years before and clearly intended, at the time of its writing, to be his *opus*. Within the space of a few years, and for good reasons, he shifted from advocacy of free trade to urging a measure of control and discrimination and back toward a multilateral system again. After attacking Lloyd George without mercy as a peacemaker he became once again his supporter in the late 20's. "The difference between me and some other people is that I oppose Mr. Lloyd George when he is wrong and support him when he is right."

The *General Theory*, however, found an audience of men that wanted to change their minds. They did not want to believe—as

Marx's predictions and the experience of the depression seemed to be forcing them to believe—that liberal capitalism must go. They might call themselves liberals or radicals or members of the left but, no less than Burke himself, they sought continuity with the past. So far as the English-speaking countries now have a reference point in the conduct of their economic policy, it is that provided by Keynes. Keynes triumphed not because he provided a platform for radicals but because he provided men who did not really want to be radicals with a plausible form of conservatism.

IN THE early 30's, long before Keynes had a perceptible influence on the ideas underlying American economic policy, the Hearst papers were campaigning for large public-works expenditures financed by borrowing—a policy of deficit financing. Very possibly the imperative of depression would have forced governments to adopt such expedients even had Keynes never lived. At a minimum, however, Keynes provided a systematic rationalization of what would otherwise have been acts of political desperation.

He also made it clear that depression remedies were only for depression. While Keynes was undoubtedly moved to write partly by the pain and suffering of these years, nothing was further from his mind than the production of a homeopathic formula to eliminate unemployment that would be invoked at all times and under all circumstances in the future. However, in the context in which Keynes wrote it was perhaps inevitable that his name should become inextricably and all but exclusively associated with defenses against depression.

But since the early 40's it is with inflation, not depression, that all Western governments have been contending. So far as there has been hardship resulting from economic instability it has been the result of rising prices, not unemployment. Yet the experience of the 30's burned itself into the minds of Americans and Western Europeans and left them subject to what can only be called a depression psychosis. Even amidst

inflation they have continued to brace themselves for the inevitable slump.

One consequence has been to identify a very large number of government policies with Keynesian remedies for depression. There are still people who believe that current defense expenditures are a disguised measure for maintaining the economy at full employment. There are many more who believe that the salvation of modern capitalism consists in finding a large and increasing number of objects for public expenditure. The name of Keynes is unhesitatingly and quite falsely invoked in support of these propositions. In fact, under the stress of war, postwar rehabilitation of capital plant and of producer's and consumer's stocks of goods, and more recently of a new defense effort, the total of public and private investment during the last ten years has been regularly pressing upon our capacity to save. This is the reason we have been plagued, recurrently, by inflation. It is a condition which is the exact reverse of that—of efforts to save in excess of desire to invest—with which Keynes identified depressions. To suppose that during the last ten years a deliberate policy of government spending has been necessary, is to think that our struggle against inflation should be made more difficult in order to prevent a notably non-existent depression. Keynes, who never suffered fools gladly, would have dealt harshly with any alleged follower who espoused such nonsense.

A further consequence of the depression psychosis is that our defenses against depression are in far better shape than our defenses against inflation. This is partly the fault of Keynes, although it is far more the result of the misdirected emphasis of his interpreters. In principle the Keynesian remedies for economic instability were symmetrical. In depression the government supplemented private demand by spending more than it took in. In times of inflation it did just the opposite—it reduced private demand by taking more in taxes than it spent.

But when the inflationary tensions are caused by war or defense expenditures, the remedies are not symmetrical and the pre-

occupation with depression has kept us from seeing this. When inflationary spending is induced by the requirements of war or rearmament, the government does not have the option of reducing expenditures to reduce demand. Accordingly its principal recourse, if the demands on the economy are to be kept within the limits of what the economy can supply, is to taxation. The taxes required may be greater than people think decent, and politicians, wise.

Moreover, when a modern economy is using the full capacity of its plant and labor force, there is a tendency for inflation to develop a dynamic of its own. Wages shove up prices and higher prices become a cause and a justification of higher wages. During the war and again in these last months of quasi-peace, we have resorted to direct wage and price controls to break the continuity of this wage-price spiral. The need for such controls was not envisaged by Keynes; the preoccupation of Keynesian economics with depression has meant that inflation control has been handled by improvisation.

Keynes did not, in other words, provide a formula for solving all of the problems of an effective and stable capitalism. Far from it. But in addition to his very considerable contribution to the substance of economics and economic policy, he had what may well prove to be an even more important effect on attitudes toward economic problems. With the change in view toward capitalism in the large, there developed, naturally enough, the conviction that any particular problem of its behavior could be solved. Thus, even though the control of inflation is still a decidedly unsolved problem, there are few economists who suppose that it must remain so.

This notion that capitalism can be (and must be) managed is still repugnant to numerous conservatives. To the extent that Keynes is responsible for it, it is another reason for resenting him. But the man who is tempted to wish that Keynes had never lived ought to remind himself that many who, as a result of his writings, now believe in a managed capitalism, might otherwise still be of the conviction that it has no future at all.

FOR ALL WHO MARCH

ALLEN MANDELBAUM

*"Neither shalt thou
go up by steps unto mine altar
that thy nakedness
be not uncovered thereon."*

WE, THE meek,
approaching the altar with
faltering steps,
take heed of the bareness and evil of our skin,
move duly, Lord, in semblance
of equilibrium.

*We need but the smoke
of bullocks in the temple-yard,
the tocsin of the Levites' reeds,
costus, galbanum, or nard,
to feed Thy Word.*

But now the altar is decay
and acrid now the altar in
the evening of the carnal day.

*"As new wine-skin that hath no vent,
at ferment-verge of bitterness,
the heart, o God of Battles, bursts,
the veil of skin lies rent.*

The searing scent of the charred
is the scent of our own flesh-souls;
not sacrificial lambs, but we have been
burnt whole.

ALLEN MANDELBAUM's translations of Hebrew poems have appeared in previous issues of COMMENTARY. He was born in 1926, and holds an MA degree from Columbia University.